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Supreme Court, U.S.
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No. 93-2098

In The

Supreme Court of the United States

October Term, 1994

C.L. GRIMES and G.W. HOLBROOK, on their own behalf and on behalf of all persons similarly situated,

Petitioners,

v.

VITALINK COMMUNICATIONS CORPORATION, a Corporation; NETWORK SYSTEMS CORPORATION, a Corporation; LESLIE G. DENEND, J. DANIEL MCCRANIE, CHARLES J. ABBE, HARRY T. REIN, and LYLE D. ALTMAN,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Third Circuit

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

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Dated: July 29, 1994

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QUESTIONS PRESENTED

1. Are the Petitioners barred under the principles of *res judicata* from challenging in a subsequent action the authority of a state court to release claims within the exclusive jurisdiction of the federal courts where the state court gave Petitioners a full and fair opportunity to challenge that court's authority to issue such a release?

2. Does a state court have authority to approve a settlement of a class action that releases claims within the exclusive jurisdiction of the federal courts where such claims arose out of the same nucleus of operative facts that gave rise to the state claims?

3. Are the Petitioners barred under the doctrine of collateral estoppel from relitigating the adequacy of representation, the fairness of a settlement and the materiality of certain disclosures made in connection with a tender offer and merger after these issues were actually litigated and finally determined in a state court judgment?

LIST OF PARENT COMPANIES AND NON-WHOLLY OWNED SUBSIDIARIES

Respondent Network Systems Corporation has no parent company and no non-wholly owned subsidiaries.

The parent company of Respondent Vitalink Communications Corporation is Network Systems Corporation, which has no non-wholly owned subsidiaries.

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BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

OPINIONS AND JUDGMENTS BELOW

This Petition arises out of an Order and Final Judgment of the Delaware Court of Chancery dated November 15, 1991 (the "Delaware Judgment") approving the settlement (the "Settlement") of a consolidated class action captioned *In re Vitalink Communications Corp. Shareholders Litig.*, Consolidated C.A. No. 12085 (Del. Ch.) (the "Delaware Action"). The Delaware Judgment and related 39-page Memorandum Opinion of the Delaware Court of Chancery are unreported but are reproduced at P91a[1] and P53a-87a, respectively. The Delaware Judgment was affirmed by the Supreme Court of Delaware on April 30, 1992 (R1a-2a). On October 5, 1992, the United States Supreme Court denied a petition for a writ of certiorari to the Supreme Court of Delaware (the "First Petition") filed by one of the Petitioners herein. *Grimes v. John P. McCarthy Profit Sharing Plan*, 113 S. Ct. 179 (1992).

Less than a month after the Delaware Supreme Court affirmed the judgment of the Court of Chancery, and before the First Petition was filed, the Petitioners filed an action under §§ 10(b) and 14(e) of the Securities Exchange Act of 1934. The United States District Court for the Eastern District of Pennsylvania granted the Respondents' motion for summary judgment and dismissed the case on February 27, 1993. (P90a) In its opinion, the district court held that the Delaware Judgment barred the federal securities law action on the grounds of release and collateral estoppel. (P42a-52a) On March 9, 1994, the United States Circuit Court of Appeals for the Third

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[1] References to the Petition are cited hereinafter as "P___"; references to Petitioners' appendix are cited as "P___a"; and references to the appendix attached hereto are cited as "R___a."

Circuit affirmed the district court order. (P88a-89a; P1a-41a)

JURISDICTION

The Supreme Court has jurisdiction over this case by virtue of 28 U.S.C. § 1254. This Court should not exercise jurisdiction under Supreme Court Rule 10 because the Petitioners fail to present any unsettled issues of federal law or any issues of federal law that are in conflict among the courts of appeals.

SUMMARY OF ARGUMENT

The Petitioners brought a federal securities law action in the United States District Court for the Eastern District of Pennsylvania challenging certain disclosures made in connection with a tender offer (the "Offer") for the common stock of Vitalink Communications Corporation ("Vitalink") and a subsequent merger (the "Merger") of Vitalink into Network Systems Corporation ("NSC"). These same transactions were the subject of an earlier class action in which the Delaware Court of Chancery, after approving the Settlement, entered a judgment over the objections of, among others, Petitioner Charles L. Grimes and Gadfly Foundation Inc., a foundation for which Grimes serves as Trustee.

In a 39-page opinion, the Court of Chancery rejected Petitioner Grimes' objections concerning the adequacy of representation of class counsel, the fairness of the Settlement, and the disclosures accompanying the Offer and Merger. The court entered an order releasing all claims arising out of the Offer, Merger and Settlement of the action. On appeal, the Delaware Supreme Court rejected Petitioner Grimes' contentions and affirmed the judgment

on the basis of the Chancery Court's "well-reasoned memorandum opinion. . . . " The United States Supreme Court thereafter denied certiorari after Petitioner Grimes filed his First Petition.

After the Delaware Supreme Court affirmed the Chancery Court's judgment, Petitioner Grimes changed lawyers, added Petitioner Holbrook and brought this action. In response to the Respondents' motion to dismiss, the Petitioners argued that the Delaware court did not have subject matter jurisdiction to release the Petitioners' federal claims asserted in the district court. They also reasserted claims attacking the adequacy of representation, the fairness of the Settlement and the disclosures made in connection with the Offer and Merger. All of these claims were released by the Delaware Judgment.

The Petitioners' challenges are barred by the full faith and credit statute. 28 U.S.C.A. § 1738. The statute bars collateral attacks on decisions of a state court once a party has had an opportunity to have his day in court. Here, the Petitioners had ample opportunity to present evidence and air their views regarding the Release, the adequacy of representation, the fairness of the Settlement and the disclosures made in connection with the Offer and Merger. Petitioner Grimes litigated these issues and lost. Petitioner Holbrook chose not to participate in the Delaware action.

Even if the full faith and credit statute did not bar the Petitioners' subject matter jurisdictional argument, their position concerning Delaware's authority to issue the Delaware Judgment containing broad releases ignores applicable law. Federal courts consistently hold that a state court may, in approving a settlement of a class action, release claims within the exclusive jurisdiction of the federal courts if the federal claims arise out of the

same factual predicate as the underlying state law claims. *See, e.g., Nottingham Partners v. Trans-Lux Corp.*, 925 F.2d 29, 32-33 (1st Cir. 1991). The Petitioners offer a distorted analysis of the case law to seek a radical departure from this well-established precedent.

The Third Circuit properly affirmed the district court's grant of summary judgment which held that the Delaware Judgment barred the federal action on the grounds of release and collateral estoppel. This Court should deny this second Petition for a Writ of Certiorari (the "Second Petition").

STATEMENT OF THE CASE

1. The Parties.

Before the Merger, Vitalink and NSC were separate, publicly held corporations. (P109a, ¶¶ 5-7) Respondents Leslie G. Denend, J. Daniel McCranie, Charles J. Abbe and Harry T. Rein (the "Vitalink Respondents") were members of the Vitalink board of directors and, as a board, recommended to the Vitalink stockholders that the stockholders accept the Offer. (P109a, ¶ 8: P111a, ¶ 14) Respondent Lyle D. Altman was a director and chairman of the NSC board of directors. (P109a, ¶ 8) After the Merger, Vitalink became a wholly owned subsidiary of NSC. (P109a, ¶ 7)

The Petitioners are former Vitalink stockholders and members of a class certified in the Delaware action. (P110a, ¶ 10) Petitioner Grimes did not tender his shares into the Offer, dissented from the Merger, and sought

appraisal of his shares.[2] (P110a, ¶ 10) Petitioner Holbrook tendered his shares into the Offer. (P110a, ¶ 10)

2. Background.

On May 6, 1991, NSC and Vitalink entered into a merger agreement in which NSC, through a wholly owned subsidiary, agreed to acquire all the common shares of Vitalink in a two-step transaction (the "Merger Agreement"). (P111a, ¶¶ 12-13) The Offer and the Merger formed the two steps of the transaction. (P110a-111a, ¶ 11) NSC agreed to pay $10.50 per share in cash for the Vitalink stock in both the Offer and the Merger.

The NSC subsidiary commenced the Offer on May 13, 1991. (P111a, ¶ 13) On that same day, Denend sent a letter to the Vitalink stockholders recommending that they accept the Offer (the "Denend Letter"). (P111a, ¶ 14) The Denend Letter informed the Vitalink stockholders that the Vitalink board had (a) unanimously approved the Offer and the Merger, (b) determined that the terms of the Offer were fair and in the best interests of the stockholders, and (c) recommended that the Vitalink stockholders accept the Offer. (P111a, ¶ 14) Attached to the Denend Letter was a copy of a Schedule 14D-9 that Vitalink filed with the Securities and Exchange Commission. The Schedule 14D-9 provided a more detailed description of the terms of the Offer and the Merger, as well as certain background facts underlying the transaction. (P111a, ¶ 15)

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[2] The Delaware appraisal action currently is stayed by agreement of the parties pending disposition of this appeal.

3. Seven Stockholder Actions Are Filed.

Shortly after the announcement of the Merger Agreement, seven Vitalink stockholders filed suit. Four suits were filed in Delaware and three in California. (P3a) The plaintiffs in these actions alleged that the Vitalink Respondents had breached the fiduciary duties they owed to Vitalink's stockholders. Some plaintiffs also charged NSC with aiding and abetting the Vitalink Respondents in their alleged breaches. (P3a) During May 1991, the parties in the Delaware actions engaged in expedited discovery in connection with a motion by the Delaware plaintiffs to enjoin preliminarily the consummation of the Offer. (P3a)

4. The Settlement.

After discovery, the parties to the Delaware and California actions agreed to settle. They executed a Stipulation and Agreement of Compromise, Settlement and Release on June 13, 1991 (the "Settlement"). (P3a) The Settlement released "[a]ll claims, rights, causes of action [and] suits" arising out of the Offer, the Merger, the accompanying disclosures or any other related event (the "Release"). (*See* P92a) The Settlement and Release were in consideration of certain benefits conferred upon the class. (P3a-4a; P58a-59a)

The Offer, as extended, expired on June 20, 1991. NSC purchased approximately 90.7 percent of the outstanding shares of Vitalink common stock in the Offer and from certain employees and former employees who exercised stock options. (P59a) The Merger was consummated on July 1, 1991. (P59a)

5. Delaware Chancery Court Approves Settlement After Considering Petitioner Grimes' Objections.

On July 18, 1991, the Delaware Court of Chancery entered an order certifying a class under Court of Chancery Rule 23(b)(1) and (2).[3] (P5a) The class included Vitalink stockholders who held Vitalink common stock between May 6, 1991 and July 1, 1991, the effective date of the Merger.[4] (P5a) The Court of Chancery also scheduled a hearing on the proposed Settlement set for September 16, 1991. (P59a)

The Petitioners were well-informed about the Settlement. NSC issued a press release on June 3, 1991, announcing the Settlement which was reported by the wire services. (R3a-7a) On July 11, 1991, NSC mailed a notice of merger that also disclosed the Settlement. (P59a) On July 29, 1991, pursuant to an order of the Court of Chancery, Vitalink mailed a Notice of Pendency of Class Action, Class Action Determination, Proposed Settlement, Settlement Hearing and Right to Appear (the "Notice") to all record holders who held Vitalink stock between May 6, 1991, and July 1, 1991, informing them, among other things, that the Chancery Court had scheduled a settlement hearing on September 16, 1991, and that they had a right to object to the Settlement. (P59a)

On September 6, 1991, Petitioner Grimes, along with several other stockholders, entered an objection to the Settlement. (P5a) Before the Settlement hearing, Petitioner Grimes submitted a 45-page memorandum of law in support of his objections. At the hearing, Petitioner

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[3] This rule is virtually identical to Federal Rules of Civil Procedure 23(b)(1) and (2).

[4] The Petitioners brought this action on behalf of the same class. (P116a, ¶ 29)

Grimes appeared through counsel and presented oral argument. Petitioner Grimes attacked the fairness of the Settlement, claiming that it conferred "absolutely no benefits" but would "force upon the class a broad release that will forever bar it from asserting any claims against the named defendants. . . . " (R11a) Among the "strong claims" that Petitioner Grimes argued would be released by the Settlement for "illusory consideration" were claims that the Vitalink Respondents breached their duty of candor under Delaware law and violated the federal securities laws. (*See* R12a, R16a; P75a)

Petitioner Grimes' principal disclosure claims attacked Vitalink's Schedule 14D-9 under federal and state law for failing to provide details about the analysis performed by Vitalink's financial advisor, Kidder, Peabody & Co. Incorporated ("Kidder"), and about the methodology utilized by Vitalink in conducting a search for potential partners. Petitioner Grimes contended that the Vitalink Respondents violated their disclosure duties for the following reasons:

> "the Offer to Purchase and Schedule 14D-9 did not discuss or summarize Kidder's valuation analysis and its limitations nor did they contain a summary of the various valuation ranges that Kidder calculated";
>
> they failed "to inform [Vitalink] stockholders that they were not soliciting bids from third parties" and thus failed to canvass the market; and
>
> they caused a deletion of a sentence from a draft of a Kidder financial opinion which had stated that Kidder has " 'not been [requested] to, and did not solicit third party indications of interest in acquiring all or any part of the Company.' "

(*See generally* P75a-80a)

On November 8, 1991, six weeks after the settlement hearing, the Court of Chancery issued a comprehensive 39-page memorandum opinion that rejected Petitioner Grimes' arguments and approved the Settlement. (P53a-85a) This opinion is a model of careful judicial scrutiny. The court considered each of Petitioner Grimes' arguments in support of his contention that the Settlement offered no value to the class in return for the released claims. The court concluded that the claims being released were "very weak" and that the record was sufficiently developed to warrant approval of the Settlement as "fair and reasonable. . . . " (P82a) In particular, the court, relying on the standards enunciated in *TSC Indus. v. Northway, Inc.*, 426 U.S. 438, 449 (1976), held that the purported nondisclosures were not material or misleading. (P77a-80a)

The Court of Chancery also evaluated the Delaware plaintiffs' application for attorneys' fees and expenses. (P82a-85a) The court found that the fee request was reasonable. The court considered the contingent nature of the fee, the quality of legal services, the standing and ability of counsel, as well as public policy considerations. (P85a) Overall, the court concluded that the services provided by class counsel were "expeditious and effective." (P84a) The court entered an Order and Final Judgment approving the Settlement, dismissing the claims with prejudice and releasing any and all further claims relating to or arising out of the Offer, the Merger, the disclosures accompanying them *and* the Settlement itself. (P91a-93a)

6. Petitioner Grimes' Appeals Are Rejected By The Delaware Supreme Court And The United States Supreme Court.

Shortly thereafter, Petitioner Grimes appealed the Delaware Judgment to the Delaware Supreme Court.

After briefing and oral argument, the Delaware Supreme Court issued an order affirming the judgment of the Court of Chancery on the basis of that court's "well-reasoned memorandum opinion. . . . " (R1a-2a)

Petitioner Grimes filed his First Petition with this Court claiming that the proceedings in the Delaware courts violated due process. Petitioner Grimes argued that these courts did not develop an adequate record from which to consider whether the absent class members were adequately represented. (P6a) The Court denied the First Petition on October 5, 1992. *Grimes v. John P. McCarthy Profit Sharing Plan*, 113 S. Ct. 179 (1992).

7. The Petitioners File Suit In District Court.

Less than a month after the Delaware Supreme Court affirmed the judgment of the Court of Chancery, and before Petitioner Grimes filed his First Petition, the Petitioners filed this action in the United States District Court for the Eastern District of Pennsylvania under Sections 10(b) and 14(e) of the Securities Exchange Act of 1934. 15 U.S.C. §§ 78j and 78n(e). Like the Petitioners' claims in the Delaware state action, their federal claims in the district court were based on the public disclosures surrounding the Offer and Merger, and they challenged many of the same disclosures that the Delaware court found to be not misleading. (P112a-114a, ¶ 17; P115a, ¶ 25)

8. The District Court Grants Summary Judgment In Favor Of The Respondents.

Vitalink, NSC and the individual Respondents moved to dismiss this action based on the Delaware Judgment. (P6a) The Petitioners asked the court below to treat the

Respondents' motion as one for summary judgment, submitted several documents of their own, and cross-moved for summary judgment. (P6a-7a) The district court held that the Petitioners were barred from maintaining their claims in this action by the Release and Delaware Judgment. (*See* P48a; P50a) The district court found that the Petitioners were members of a class who were bound by the Release issued in the Delaware Judgment which barred all claims, including claims under federal securities laws. (P48a) Second, and alternatively, the district court found that the issues raised by the federal securities action were barred by collateral estoppel, because the predicate facts that underlie the federal case, which primarily involve issues of nondisclosure, overlap with the facts underlying the state court proceeding. (P50a) The district court also examined the Petitioners' allegation that they were denied due process in the state court proceedings and concluded that this claim simply did "not jive with the record." (P51a) Accordingly, the district court granted summary judgment in favor of the Respondents. (P51a-52a)

9. The Third Circuit Affirms The District Court's Judgment.

As discussed in greater detail *infra*, the United States Court of Appeals for the Third Circuit affirmed the district court's judgment on March 9, 1994. The panel for the Third Circuit unanimously affirmed the district court's ruling that the Delaware Court of Chancery could enter an order releasing all claims, including federal securities claims. The Third Circuit also affirmed the district court's ruling that the Petitioners' action was barred by the collateral estoppel effect of the Delaware Judgment. (*See* 19a)

Circuit Judge Hutchinson concurred with the Third Circuit's holding that Petitioner Grimes was barred from maintaining this action, but dissented with respect to Petitioner Holbrook stating that Petitioner Holbrook was not bound by the Delaware Judgment because the Delaware courts lacked personal jurisdiction over him. (*See* P23a)

REASONS FOR DENYING THE WRIT

The Petitioners contend that this Court should approach their Petition "from the crucial viewpoint of the Delaware Chancery Court's *subject matter* jurisdiction" and not "from the irrelevant viewpoint of . . . *personal* jurisdiction" over the Petitioners. (P7) They argue that the question of a state court's ability to release claims within the exclusive jurisdiction of the federal courts "is far and away the most important aspect of the case." (P17) However, *res judicata* bars the Petitioners from raising this issue. In addition, even if they could raise it, well-established authority shows that the Delaware Court of Chancery had authority to approve a settlement releasing claims within the exclusive jurisdiction of the federal courts. No split of authority exists among the circuits concerning whether a state court can release federal claims in a settlement agreement.

Furthermore, the doctrine of collateral estoppel bars the Petitioners' arguments relating to the adequacy of representation, the fairness of the Settlement and the disclosures made in connection with the Offer and Merger. The Delaware courts provided the Petitioners with all well-recognized due process protections, carefully considered all contentions and properly found that the record was sufficiently developed to approve the

Settlement. The Petitioners' newly fashioned constitutional attack of Delaware's law on issue preclusion is belated, without merit and not worthy of this Court's consideration.

Finally, the Petitioners' concession that the issue of personal jurisdiction is "irrelevant" is fatal to their Petition. Even if the issue of personal jurisdiction were relevant, the record below establishes that Delaware had sufficient contacts with the Petitioners to exercise personal jurisdiction over them and to release the claims. The Petitioners fail to show any authority to rebut Delaware's assertion of personal jurisdiction or to discuss authority relied on by the district court and Third Circuit supporting the Delaware Court of Chancery's exercise of jurisdiction over the Petitioners.

A. THE DELAWARE COURT OF CHANCERY'S DECISION TO RELEASE THE FEDERAL SECURITIES CLAIMS IS ENTITLED TO FULL FAITH AND CREDIT UNDER THE DOCTRINE OF RES JUDICATA.

The Petitioners argue that the Court of Chancery had no power to approve a settlement releasing claims within the exclusive jurisdiction of the federal courts. This claim is barred by the full faith and credit due the Delaware Judgment. The " 'principles of *res judicata* apply to questions of jurisdiction as well as to other issues.' " *Underwriters Nat'l Assurance Co. v. North Carolina Life & Accident & Health Ins. Guar. Ass'n*, 455 U.S. 691, 706 (1982). Once a party has had an opportunity to present his view of the law in one action, a subsequent collateral attack on the jurisdiction of the first court is not permitted. *Id.* at 706 n.13. Such an attack would "merely retr[y] the issue[s] previously determined" and undermine "[t]he need for

finality [, that] applies with equal force to questions of jurisdiction." *Id.*

The Delaware court gave the Petitioners a full and fair opportunity to challenge that court's authority to release the class federal disclosure claims. Like the North Carolina Association in *Underwriters Nat'l*, they received notice of the Settlement which fully disclosed that the Settlement would release all claims arising out of the transaction. *Id.* at 707. Under *Underwriters Nat'l*, the Petitioners were "obliged to advance [their] argument" that the Delaware court "did not have the authority to settle" the federal claims when they were given the opportunity to do so. *Id.* at 710.

Petitioner Grimes argued, and the Court of Chancery considered, that the Settlement would release the class federal disclosure claims. (P75a) Yet, Petitioner Grimes did not challenge the Delaware courts' jurisdiction to grant the Release. Petitioner Holbrook chose to do nothing. "A party cannot escape the requirements of full faith and credit and res judicata by asserting its own failure to raise matters clearly within the scope of a prior proceeding." *Underwriters Nat'l*, 455 U.S. at 710. Moreover, if they had raised the issue, the Delaware Chancery Court would have been required to follow the Delaware Supreme Court's precedent in *Nottingham Partners v. Dana*, 564 A.2d 1089, 1104 (Del. 1989), holding that Delaware state courts possess subject matter jurisdiction to dismiss federal claims as part of a settlement agreement. The Petitioners cannot now raise this subject matter jurisdiction argument in the federal courts.

B. FEDERAL COURTS HAVE UNIFORMLY RECOGNIZED THE POWER OF STATE COURTS TO RELEASE CLAIMS WITHIN THE EXCLUSIVE JURISDICTION OF THE FEDERAL COURTS.

Even if the Petitioners could challenge the Delaware Chancery Court's jurisdiction to release their claims, the challenge would fail because state courts have the power to release federal claims. Indeed, the Third Circuit below held "that as a matter of federal law a state court has the power to enter a settlement negotiated by the parties as a judgment which releases exclusive federal claims that the state court could not itself entertain." (P21a) In so holding, the Third Circuit found that "several other federal courts . . . have recognized the broad power of state courts to approve and enforce settlements which reflect the parties' intent to release all claims arising from a transaction regardless of whether the class action court has jurisdictional competency to hear those claims." *Id.*; *see generally Nottingham Partners*, 925 F.2d at 34; *Abramson v. Pennwood Inv. Corp.*, 392 F.2d 759, 762 (2d Cir. 1968); *Sandler Assocs., L.P. v. BellSouth Corp.*, 818 F. Supp. 695, 704-05 (D. Del. 1993), *aff'd mem.*, No. 91-1447, 1994 U.S. App. LEXIS 12569 (3d Cir. Apr. 12, 1994); *Lowenschuss v. Resorts Int'l, Inc.*, No. 89-1071, 1989 U.S. Dist. LEXIS 7407, at *20 n.15 (E.D. Pa. June 29, 1989), *aff'd mem.*, 947 F.2d 936 (3d Cir. 1991).

In facts remarkably similar to the facts of this case, the First Circuit, in *Nottingham*, found that:

> as a general matter, federal courts recognize that a court can approve a settlement agreement embodying terms which the court would ordinarily have no power to promulgate. . . . Hence, as a matter of federal law, a state court can approve and enforce a settlement which requires

> a party to release claims actually brought, or potentially "bringable," in federal court under "exclusive jurisdiction" federal statutes even though the state court could not adjudicate claims arising under such statutes. *See TBK Partners[, Ltd. v. Western Union Corp.*], 675 F.2d [456,] 460 [(2d Cir. 1982)]; *Abramson v. Pennwood Inv. Corp.*, 392 F.2d 759, 762 (2d Cir. 1968); *Seagoing [Uniform Corp. v. Texaco, Inc.]*, 705 F. Supp. [918,] 923 [(S.D.N.Y. 1989)]. And where, as here, the federal law claims to be released stemmed from the same nucleus of operative fact as the state law claims, the release could legitimately be used as a defense to the former in a federal venue.

925 F.2d at 34.

Other federal circuit courts have recognized, like the First and Third Circuit, that a court may approve a release of claims which are outside the jurisdiction of the issuing court. For instance, the Second Circuit has ruled several times that a court may approve such a settlement. *See TBK Partners, Ltd. v. Western Union Corp.*, 675 F.2d 456, 460 (2d Cir. 1982) (collecting cases). Similarly, the Ninth Circuit, explaining that the breadth of settlement negotiations is not necessarily confined by the pleadings, held that a district court need not have subject matter jurisdiction over claims to approve their release. *Class Plaintiffs v. City of Seattle*, 955 F.2d 1268, 1287-89 (9th Cir.), *cert. denied*, 113 S. Ct. 408 (1992). The Fifth Circuit endorsed the same principle by stating "[t]he weight of authority establishes that in such a case, a court may release not only those claims alleged in the complaint and before the court, but also claims which 'could have been alleged by reason of or in connection with any matter or facts set forth or referred to in' the complaint." *In re Corrugated Container Antitrust Litig.*, 643 F.2d 195, 221 (5th Cir.), *aff'd*,

659 F.2d 1322 (1981), *quoting Patterson v. Stovall*, 528 F.2d 108, 110 n.2 (7th Cir. 1976).

Federal district court decisions are also in agreement. *See, e.g., Lowenschuss v. Resorts Int'l*, No. 89-1071, 1989 U.S. Dist. LEXIS 7407 (E.D. June 29, 1989); *Sandler*, 818 F. Supp. at 695. Indeed, in a recent case that is strikingly similar to this case, the United States District Court for the District of Delaware stated that federal law on this question is uniform:

> When called upon to resolve this question [the release of exclusively federal claims by a state court], *federal courts have uniformly dismissed claims*, including claims committed to their exclusive jurisdiction, that have been released in settlement of class actions brought in state courts.

Sandler, 818 F. Supp. at 704 (emphasis added). This decision was affirmed without opinion by the Third Circuit.[5] *See Sandler*, 1994 U.S. App. LEXIS 12569.

Federal recognition of state court releases and state recognition of federal releases both are based on the principles of comity and federalism underlying the full faith and credit clause. Comity serves important policy interests because it permits state courts to achieve comprehensive settlements that "prevent relitigation of settled questions at the core of a class action. . . . " *TBK Partners*, 675 F.2d at 460. As explained in *Sandler*, comity between state and federal courts is "crucial":

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[5] Commentators also agree. *See, e.g.*, 18 Charles A. Wright et al., *Federal Practice and Procedure* § 4470 at 688 (1981) ("[a]part from claim preclusion as such, settlement of state court litigation has been held to defeat a subsequent federal action if the settlement was intended to apply to claims in exclusive federal jurisdiction as well as other claims").

> To deny effect to a release of claims merely because it was given in an action commenced in state court would invite unprecedented consequences. Such a doctrine would unjustifiably proliferate litigation, defeat legitimate expectations of the settling parties, engender uncertainty among class members and defendants as to their ability to retain the benefits of settlements, discourage settlements altogether and create unwarranted conflict between state and federal courts.

818 F. Supp. at 705.

The Petitioners attempt to undercut the foregoing authority by arguing that the power of a federal court to release state claims over which it lacks subject matter jurisdiction, as in *TBK Partners, City of Seattle,* and *In re Corrugated Container,* is different from the power of a state court to release exclusively federal claims, as in *Nottingham, Sandler,* and the present case. In fact, both situations raise the same jurisdictional issues and implicate the same notions of finality in settlement negotiations. The Petitioners claim that these lines of cases are fundamentally different "[b]ecause of pendent jurisdiction." (P20) Yet, none of these cases relies on the concept of pendent jurisdiction, and their language, as shown above, includes both types of cases.

The Petitioners also argue that the Court should ignore this well-established authority and adopt a radical change in the law. They argue that a class representative in a class action in state court cannot, in reaching a settlement of that action, agree to release claims he shares in common with the class but which could not be pleaded in the complaint. (*See* P17; 25-26 (Propositions 1 and 5)) This assertion, however, ignores the fundamental principles governing class actions. "According to traditional

notions, a member of the class in a Rule 23 suit is considered to be a party by representation, and will be bound to the same extent as an actual party." 7B Charles A. Wright et al., *Federal Practice and Procedure* § 1789 at 247 (1986); *Hansberry v. Lee*, 311 U.S. 32, 41-43 (1940); *see also Fisher Bros. v. Mueller Brass Co.*, 102 F.R.D. 570, 576 (E.D. Pa. 1984) ("[c]lass members are bound by a settlement or a judgment on the merits of a class action even though they do not choose the forum or the counsel and may even be unaware of the litigation"). The class representative's authority to represent the class applies at all stages of the action and includes the power to agree to a settlement releasing all claims shared by the class. *Nottingham Partners*, 925 F.2d at 33; *Richard's Lumber & Supply Co. v. United States Gypsum Co.*, 545 F.2d 18, 21 (7th Cir. 1976), *cert. denied*, 430 U.S. 915 (1977).

The Third Circuit rejected the Petitioners' invitation to transform the law and dismantle the authority of a class action representative to bind the class. (P16a) It found the Petitioners' reliance on *National Super Spuds, Inc. v. New York Mercantile Exch.*, 660 F.2d 9, 18-19 (2d Cir. 1981), to be misplaced. (*Compare* P21a-22a *with* P25-26) In *Super Spuds*, the court held that a class representative had no power to release claims arising out of a *different factual predicate* than those pleaded in the complaint. For those cases involving the same factual predicate, however, *Super Spuds* articulated a different rule: "a settlement could properly be framed so as to prevent class members from subsequently asserting claims relying on a legal theory different from that relied upon in the class action complaint but depending upon the very same set of facts." 660 F.2d at 18 n.7.

The Second Circuit later followed *Super Spuds* when it held that a court approving a class action settlement

may release claims over which it has no subject matter jurisdiction. *TBK Partners*, 675 F.2d at 460. The court in *TBK Partners* explained that the underlying concern in *Super Spuds* was that a class representative who does not share common claims with class members might not fully advance the interests of class members with unshared claims. *Id.* at 461-62. However, the release of claims based on the same factual predicate, as in this case, does not implicate this concern. *See also Class Plaintiffs v. City of Seattle*, 955 F.2d at 1287-89.

The Petitioners also assert that the Seventh Circuit would deny the power of a state court to release claims within the exclusive jurisdiction of the federal courts. They base their argument on *General Motors*. (*See* P21, citing *In re General Motors Corp. Engine Interchange Litig.*, 594 F.2d 1106, 1134 (7th Cir.), *cert. denied*, 444 U.S. 870 (1979)) However, the Petitioners mischaracterize *General Motors*. The issue in *General Motors* was whether a federal court approved settlement agreement which included the release of state law claims was "fundamentally unfair" where class members were not notified that their participation in the class might result in release of their state law claims. Thus, *General Motors* in no way suggests that a release of claims by a federal or state court is inappropriate where, as here, class members are fairly apprised of the effects of such approval.

The Petitioners' interpretation of *General Motors* has not been endorsed by anyone but themselves. Furthermore, the Fifth Circuit rejected the Petitioners' interpretation and "read [*General Motors*] to hold that a court can approve a settlement extinguishing state claims not before it if the class members have been notified that . . . the settlement might result in release of their state claims." *In re Corrugated Container*, 643 F.2d at 221 n.40.

The Fifth Circuit recognized that "even when the court does not have power to adjudicate a claim, it may still 'approve release of that claim as a condition of settlement of [an] action [before it].' " *See id.* at 221, *quoting Abramson*, 392 F.2d at 762.

No split of authority exists among the circuits as to the issue of a state court's authority to release the Petitioners' federal claims, which is the question the Petitioners ascribe as "far and away the most important aspect of the case." (P17) For this reason, it would be inappropriate and a waste of judicial resources to grant certiorari in this case. *See Layne & Bowler Corp. v. Western Well Works, Inc.*, 261 U.S. 387, 393 (1923).

C. THE JUDGMENT IN DELAWARE IS ENTITLED TO FULL FAITH AND CREDIT AND BARS THE PETITIONERS FROM RELITIGATING THE ISSUES DECIDED IN DELAWARE UNDER THE DOCTRINE OF COLLATERAL ESTOPPEL.

The United States Supreme Court also has consistently recognized that "the judgment of a state court should have the same credit, validity, and effect, in every other court of the United States" (quotation omitted). *Underwriters Nat'l*, 455 U.S. at 704. The courts below properly found that the Delaware Judgment bars the Petitioners' claims. The judgment was rendered only after the Petitioners had an opportunity for a full and fair hearing in Delaware. As such, the full faith and credit statute collaterally estops relitigation in federal court of the same issues decided in the state court. 28 U.S.C.A. § 1738; *see also Allen v. McCurry*, 449 U.S. 90, 101 (1980).

The Third Circuit correctly followed *Marrese v. American Academy of Orthopedic Surgeons*, 470 U.S. 373, 381 (1985), which held that "the federal full faith and credit

statute can operate to bar the relitigation of issues decided by the state court, even though the state court would not have subject matter jurisdiction to consider the federal claims in the first instance. . . . " (P18a, citing *Marrese*, 470 U.S. at 380-81) The Third Circuit, relying on Supreme Court precedent, then correctly looked to the law of collateral estoppel in Delaware to see if the Petitioners were precluded from relitigating the issues raised in the Delaware Action. (*See* P18a, relying on *Migra v. Warren City Sch. Dist. Bd. of Educ.*, 465 U.S. 75, 81 (1984), and *Kremer v. Chemical Constr. Corp.*, 456 U.S. 461, 480-82 (1982))

The Third Circuit found that "Delaware follows the usual rule that a judgment in one case constitutes a final determination concerning questions of fact litigated by the parties." (*See* P20a) It also found that, under Delaware law, the "facts that underlie the federal non-disclosure claims were actually litigated during the state court proceeding and were conclusively resolved against the objectors, here the federal plaintiffs." (P17a) It further concluded that "[a]s a result [of the Delaware Court's final determination], the plaintiffs cannot relitigate in federal court the issues of non-disclosure and fairness of the settlement that were conclusively determined in the Delaware proceeding." (P18a)

The Third Circuit affirmed the district court's determination that each of the elements under Delaware state law required for collateral estoppel were present. (*See* P20a; P49a-50a) The Third Circuit's determination is supported by the record. The Delaware Chancery Court entered an Order and Final Judgment dismissing the Delaware claims. (P49a) In that action, the Court of Chancery gave all members of the class notice and full opportunity to object to the fairness of the Settlement and the

certification of the class. (*See* P46a; P49a; P50a-51a) Petitioner Grimes took advantage of this opportunity and argued at great length in the Delaware action that the Settlement was unfair.[6] He claimed that the Settlement contained only "sham" benefits because, among other things, the benefits were "illusory" and "speculative" and insufficient to "cut off forever" the ability of the absent members of the class to pursue their rights, including their purported federal claims. (*Compare* R11a; R16a; P50a-51a; and P80a-82a *with* P26 (Propositions 6 and 7))

The Court of Chancery determined the disclosure issues adversely to Petitioner Grimes. It devoted seven pages of its Memorandum Opinion to evaluating those claims under the federal materiality standard (as required

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[6] The Petitioners' argument that Petitioner Grimes had "no opportunity to contest the certification of a non-opt-out class" is unsupported. (*Cf.* P5) In fact, the Petitioners could have made such a challenge in Delaware, but did not. *Cf. Lowenschuss v. Resorts Int'l, Inc.*, C.A. No. 89-1071, 1989 U.S. Dist. LEXIS 7407 (E.D. Pa. June 29, 1989), *aff'd mem.*, 947 F.2d 936 (3d Cir. 1991) (class members in Delaware objected at settlement hearing to certification for settlement purposes of non-opt-out class). Petitioners are therefore precluded from asserting the claim under the principles of *res judicata*.

Similarly, the Petitioners failed to attack Delaware's certification in the courts below or meaningfully raise it in this Court. (*See* P25 (Proposition 4)) Furthermore, the Petitioners' half-hearted attack at P25 ignores well-reasoned case authority in which Delaware courts have recognized that actions seeking to enjoin mergers are properly certified without a right to opt out even when they include claims for monetary relief. *Nottingham Partners v. Dana*, 564 A.2d at 1089, 1097-1101 (Del. 1989); *In re Mobile Communications Corp. of Am. Consol. Litig.*, [1991-1992 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 96,558 (Del. Ch. Jan. 18, 1991), *aff'd mem.*, 608 A.2d 729 (Del.), *cert. denied*, 112 S. Ct. 3032 (1992). The Petitioners, therefore, have not presented this issue in a manner worthy of this Court's consideration.

under Delaware law) in *TSC Indus. v. Northway, Inc.*, 426 U.S. 438, 449, 96 S. Ct. 2126, 2132 (1976). It found no material omissions or misrepresentations under state and federal law. (P75a-80a)

The court also determined the Petitioners' challenges concerning the Settlement's fairness and adequacy of representation adversely to Petitioner Grimes. The court carefully weighed the value of the released claims (which it found to be "very weak") against the benefits of the Settlement and found the Settlement to be fair and reasonable. (*See* P82a) In so doing, the court specifically addressed and rejected Petitioner Grimes' claims that the benefits conveyed by the Settlement were "wholly illusory." (P80a-81a) With respect to the class representative, it found counsel to be "expeditious and effective." (P84a)

The Court of Chancery's extensive analysis is far from a "boiler-plate" approval, as suggested by the Petitioners.[7] *See McDonald v. Chicago Milwaukee Corp.*, 565 F.2d 416, 427-28 (7th Cir. 1977). The Delaware Judgment was, thereafter, affirmed by the Delaware Supreme Court. Petitioner Grimes then made many of these same arguments in his First Petition, which was denied by this Court two years ago. (*Compare* P14-19 *with* P26 (Proposition 7))

The courts below held that the Petitioners were precluded from relitigating these issues by the collateral estoppel effect of the Delaware Judgment, which is entitled to full faith and credit in this action. (P19a; P50a) These holdings are consistent with established authority.

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[7] As in the First Petition, the Petitioners also complain that the plaintiffs were awarded attorney fees and expenses totalling $275,000. (P4) Yet, Petitioner Grimes did not oppose the fee application in his 46-page memorandum opposing the Settlement, and at oral argument Grimes' counsel stated that the objectors took no position regarding the requested fee.

See Boothe v. Baker Indus., 262 F. Supp. 168, 174 (D. Del. 1966) (refusing to relitigate issues decided by a state court in support of a judgment approving a settlement); *Green v. Ancora-Citronelle Corp.*, 577 F.2d 1380, 1383 (9th Cir. 1978) (dismissing Securities Exchange Act claims on ground of collateral estoppel based on a judgment in a state action following a settlement).[8]

Because Petitioner Grimes appeared and objected to the Settlement, he is precluded from relitigating the issues decided in Delaware under the doctrine of collateral estoppel. *Hansberry*, 311 U.S. at 42-43 ("members of a class not present as parties to the litigation may be bound by the judgment . . . where they actually participate in the conduct of the litigation"); *Dosier v. Miami Valley Broadcasting Corp.*, 656 F.2d 1295, 1299 (9th Cir. 1981); *Robertson v. National Basketball Ass'n*, 622 F.2d 34, 36 (2d Cir. 1980); *In re Antibiotic Antitrust Actions*, 333 F. Supp. 296, 298 (S.D.N.Y.), *aff'd sub nom., Connors v. Chas. Pfizer & Co.*, 450 F.2d 1119 (2d Cir.), *cert. denied*, 408 U.S. 930 (1972).

Because Petitioner Holbrook's interests were represented by Petitioner Grimes, he, too, is precluded from relitigating these issues under the doctrine of collateral estoppel. *See Garcia v. Board of Educ.*, 573 F.2d 676, 679 (10th Cir. 1978) ("[t]o the extent [absent class members']

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[8] *See also Kaufman v. BDO Seidman*, 984 F.2d 182, 185 (6th Cir. 1993) ("plaintiffs' [federal securities law] claims are barred by the preclusive effects of the Michigan jury's decision"); *Murphy v. Gallagher*, 761 F.2d 878, 886 (2d Cir. 1985) (findings of fact in New York action "dispose[d] of the entire federal [securities law] action"); *cf. Allen v. McCurry*, 449 U.S. at 101 n.17 (the concerns addressed in *England v. Louisiana State Bd. of Medical Examiners*, 375 U.S. 411 (1964), have "no bearing whatsoever" on the preclusive effect in federal court of a prior judgment in state court).

interests were not represented by the . . . plaintiffs . . . they were certainly vigorously presented and pursued by the intervenors"); *accord Wilder v. Thomas*, 854 F.2d 605, 620-21 (2d Cir. 1988) (where the issues raised in two actions were such that they did not vary according to individual plaintiffs, a plaintiff in the second action was found to be in privity with co-plaintiffs who had litigated the same issues in the first action). Thus, the Petitioners are barred under the doctrine of collateral estoppel from relitigating the issues considered and rejected by the Delaware courts.[9]

The Petitioners ask this Court to reevaluate the Delaware law of collateral estoppel, claiming in a generalized manner that it somehow violates the federal constitution. (*See* P22-23 (Proposition 2)) As discussed above, however, Delaware follows the same principle as other jurisdictions, *see supra* 22, 25, which furthers the intent of, and is consistent with, the full faith and credit statute.

Furthermore, the Petitioners failed to raise this constitutional attack in the courts below. The Court, therefore, should refrain from considering whether the

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[9] In the Third Circuit, the Petitioners claimed that they had an absolute right under the Third Circuit's decision in *In re Real Estate Title & Settlement Servs. Antitrust Litig.*, 869 F.2d 760 (3d Cir.), *cert. denied*, 493 U.S. 821 (1989), to relitigate the validity of the Settlement and adequacy of representation in the forum of their choice. The Third Circuit and the district court rejected this argument. (P15a-16a; P46a-47a) The Petitioners' continued reliance on this case in an unspecified manner in the Second Petition (P27) should also be rejected by the Court. Similarly, the Petitioners' reliance on *Martin v. Wilks*, 490 U.S. 755 (1989), is even more farfetched. (P27) That case did not involve a class action. *Martin*, 490 U.S. at 755-61. *Martin*, therefore, has no bearing on the well-settled rule that class members are bound by their representatives.

Delaware law of collateral estoppel is unconstitutional, because this Court "cannot decide issues raised for the first time" in a petition for writ of certiorari. *See Tacon v. Arizona*, 410 U.S. 351, 352 (1973). Moreover, this Court should permit the Delaware state courts to address the constitutionality of its own laws first, because "in a federal system it is important that state courts be given the first opportunity to consider the applicability of state laws in light of constitutional challenge, since the [laws] may be construed in a way which saves their constitutionality." *See Cardinale v. Louisiana*, 394 U.S. 437, 439 (1969).[10]

D. DELAWARE COURTS HAD PERSONAL JURISDICTION OVER THE PETITIONERS.

In their Second Petition, the Petitioners concede that personal jurisdiction is "irrelevant" and that subject matter jurisdiction is the "crucial" issue. (P7) Given this concession, this Court should not allow the Petitioners to reverse their position and claim that personal jurisdiction is central. Therefore, this Court should not consider the Petitioners' personal jurisdiction arguments. (*See* P24-25 (Proposition 3))

But if it were to do so, the record below establishes that Delaware had sufficient contacts with the Petitioners to create personal jurisdiction and to release the claims.

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[10] The Petitioners' generalized and broad conclusory argument that obtaining a settlement in Delaware is like obtaining a divorce in Nevada is simply unsupported by the record or by case authority. (*See* P10) Furthermore, this argument is the same type of argument presented two years ago in the First Petition and, as discussed *supra*, was barred the first time. No facts exist to suggest that the Settlement resulted from anything but an arm's-length, negotiated Settlement.

(*See* P11a-16a) The Petitioners held stock in a corporation created under, and governed by, the laws of Delaware.[11] This established sufficient contacts with Delaware for purposes of adjudicating the claims arising out of the Offer and Merger. *Hynson v. Drummond Coal Co.*, 601 A.2d 570, 579 (Del. Ch. 1991). As Chancellor Allen explained in *Hynson*:

> [T]he law has long put the buyer of corporate stock on notice that corporate rights attaching to stock ownership may be adjudicated in a single proceeding in another jurisdiction, including at a minimum the corporation's state of incorporation.

Hynson, 601 A.2d at 579 (citing *Shaffer v. Heitner*, 433 U.S. 186, 97 S. Ct. 2569 (1977) (Brennan, J., concurring in part and dissenting in part)). To bind the stockholders as an aggregate class to a determination of their rights as stockholders is entirely consistent with traditional notions of fairness. Otherwise, the directors of the corporation could never be afforded a single adjudication in which the questions of their legal and equitable obligations to the class of stockholders could be determined.[12] *Hynson*, 601 A.2d at 579.

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[11] Petitioner Grimes had additional contacts because he personally appeared in Delaware and objected to the Settlement. (P5a)

[12] This Court has recognized this same principle in the area of trust law. Non-resident beneficiaries of a trust may be bound by an adjudication of the trustee's duties in the jurisdiction that is the situs of the trust. *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306, 312-13 (1950). The relationship of stockholders to a corporation is the same as the relationship of beneficiaries to a trust. Indeed, the fiduciary duties of corporate directors are rooted in the fiduciary duties of trustees. *Hynson*, 601 A.2d at 575.

The Petitioners chose to ignore *Hynson* in the Second Petition. The fact that the Petitioners ignored this precedent that establishes personal jurisdiction over them further underscores the weakness of the Petitioners' attack on the Delaware courts' exercise of personal jurisdiction. Furthermore, in the courts below, the Petitioners accepted *Hynson*'s holding that a state court may exercise personal jurisdiction over corporate stockholders, such as Holbrook, for the purpose of adjudicating internal corporate rights created by state law. (R18a-19a)

In the courts below, however, the Petitioners attempted to narrow *Hynson* by limiting its application to state law claims. (*See* R19a) This argument, however, confuses the power of the Delaware court to exercise personal jurisdiction in the first place with the power of the court after it has already exercised personal jurisdiction. Here, the Court of Chancery properly exercised personal jurisdiction over Holbrook for purposes of adjudicating his duty of candor claim. After exercising personal jurisdiction over him, the Court of Chancery then properly exercised its power to release federal disclosure claims arising out of the same factual predicate. Petitioner Holbrook was notified of the scope of the Release. Therefore, he could reasonably anticipate that the court would exercise its power to release his federal claims. Moreover, because of the close nexus between the state and federal claims, the court's decision to release the federal claims is fair. Both the state and the federal claims arose out of a common nucleus of operative facts, and the court's decision to release them together imposed no additional hardship. *Cf. Oxford First Corp. v. PNC Liquidating Corp.*, 372 F. Supp. 191, 196 n.15 (E.D. Pa. 1974) (the court in a federal securities fraud action may exercise personal jurisdiction over pendent state law claims

because it imposes no additional hardship on defendant to litigate both claims). Thus, the courts below correctly held that the Petitioners were bound by the Delaware Judgment.

CONCLUSION

For all of the foregoing reasons, the Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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DATED: July 29, 1994

No. 93-2098

In The

Supreme Court of the United States

October Term, 1994

C.L. GRIMES and G.W. HOLBROOK, on their own behalf and on behalf of all persons similarly situated,

Petitioners,

v.

VITALINK COMMUNICATIONS CORPORATION, a Corporation; NETWORK SYSTEMS CORPORATION, a Corporation; LESLIE G. DENEND, J. DANIEL MCCRANIE, CHARLES J. ABBE, HARRY T. REIN, and LYLE D. ALTMAN,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Third Circuit

APPENDIX TO BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

IN THE SUPREME COURT OF THE
STATE OF DELAWARE

CHARLES L. GRIMES, JOHN D. BURTON, REED RUBIN, LOUISE I.G. IRELAND, RENATE WINSTON (as custodian for HELLA WINSTON), WILLIAM P. WOOD, JR., LOUISA W. RUBY, CHARLES KELLY, GADFLY FOUNDATION, INC. and FIDELITY BANK (as custodian for GORDON W. CHAPLIN and for SUSAN C. STERNBERG),	§	No. 468, 1991
Objectors Below, Appellants,	§	Court Below – Court of Chancery of the State of Delaware, in and for New Castle County C.A. No. 12085
v.	§	
JOHN P. McCARTHY PROFIT SHARING PLAN,	§	
Plaintiff Below, Appellee.	§	
and	§	
VITALINK COMMUNICATIONS CORPORATION, LESLIE DENEND and NETWORK SYSTEMS CORPORATION,	§	
Defendants Below, Appellees.	§	

Submitted: April 28, 1992
Decided: April 30, 1992

Before HORSEY, MOORE and HOLLAND, Justices.

ORDER

This 30th day of April, 1992, the Court having considered this matter after oral argument and upon the briefs filed by the parties, and having concluded that the same should be affirmed on the basis of and for the reasons assigned by the Court of Chancery in its well-reasoned memorandum opinion dated November 8, 1991 and its order and final judgment dated November 15, 1991.

NOW, THEREFORE, IT IS HEREBY ORDERED that the judgment of the Court of Chancery be, and the same hereby is,

AFFIRMED.

BY THE COURT:

/s/ Randy J. Holland
Justice

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June 3, 1991, Monday

SECTION: Financial News

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HEADLINE: NETWORK SYSTEMS CORP. AND VITALINK COMMUNICATIONS CORP. ANNOUNCE EXTENSION OF OFFER AND SETTLEMENT OF DELAWARE SHAREHOLDER ACTIONS

DATELINE: MINNEAPOLIS and FREMONT, Calif., June 3

KEYWORD: DC- network-systems

BODY:

Network Systems Corporation (NASDAQ: NSCO) and Vitalink Communications Corporation (NASDAQ: VITA) today announce that the expiration date of Network Systems' tender offer to purchase all outstanding shares of common stock of Vitalink has been extended from Monday, June 10, 1991 at 12:00 a.m. (EST), to Thursday, June 20, 1991 at 12:00 a.m. (EST). The offer was extended pursuant to the terms of a settlement agreement effective as of May 31, 1991, with respect to the putative class action lawsuits filed in the Court of Chancery of the State of Delaware, New Castle County, against Vitalink, Vitalink's chairman and Network Systems in connection with Network Systems' proposed acquisition of Vitalink. While Vitalink and Network continue to believe that the

claims asserted are without merit, they agreed to the settlement to avoid further expense and distraction from the lawsuits.

The settlement agreement provides that Network Systems' option, under certain circumstances, to acquire slightly less than 20 percent of Vitalink's outstanding common stock will be amended to permit Vitalink to cancel the option by making a cash payment. Any such payment, and any payment in connection with network Systems' election to cancel the option, will not exceed $2.77 million. Pursuant to the settlement agreement, the merger agreement will be amended to limit Vitalink's obligation to reimburse Network Systems for its fees and expenses in certain circumstances to $1.75 million. The settlement agreement also provides for, subject to the approval of the Delaware Chancery Court, dismissal with prejudice of the Delaware lawsuits.

The depositary for the offer has advised Network Systems that through May 30, 1991, approximately 377,500 shares of Vitalink common stock had been tendered.

Founded in 1980, Vitalink is a supplier of internetworking systems used to build large, multivendor computer networks.

Network Systems, based in Minneapolis, makes high performance data communications systems. CONTACT: Richard A. Fisher of Network Systems, 612-424-4888; or Wes Saia of Vitalink, 415-794-1100

* * *

2ND STORY of Level 1 printed in FULL format.

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June 3, 1991, Monday, BC cycle

SECTION: Financial Report.

LENGTH: 179 words

HEADLINE: NETWORK SYSTEMS EXTENDS VITALINK <VITA.O> OFFER

DATELINE: MINNEAPOLIS, JUNE 3, REUTER

BODY:

Network Systems Corp <NSCO.0> said it extended its tender offer to purchase all of the outstanding shares of Vitalink Communications Corp until 0001 EDT/0401 GMT on June 20.

The offer previously had been set to expire at the same time on June 10. Network Systems said it extended the offer as part of an agreement to settle class action lawsuits filed in Delaware Chancery Court against Vitalink, Vitalink's chairman and Network Systems.

While Network and Vitalink continue to believe that claims asserted are without merit, they agreed to the settlement to avoid further expense and distraction.

The settlement agreement provides that Network Systems' option to acquire slightly less than 20 pct of Vitalink's outstanding common will be amended to allow Vitalink to cancel it by making a cash payment. Any such payment will not exceed 2.77 mln dlrs, it said. The merger agreement will also be amended to limit Vitalink's obligation to reimburse Network Systems for fees and

expenses to 1.75 mln dlrs. As of May 30, 377,500 shares of Vitalink had been tendered.

DOCUMENT- 3 OF 5

190603-1684.
Network Systems Extends Vitalink Bid To June 20
06/03/91
DOW JONES NEWS WIRE (DJ)

- NSCO VITA

MINNEAPOLIS -DJ- Network Systems Corp. and Vitalink Communications Corp. said the expiration date of Network Systems' tender offer to purchase all outstanding common shares of Vitalink was extended to June 20 from June 10.

- The extension is part of a settlement with respect to the class action lawsuits filed in the Court of Chancery in Delaware against Vitalink, its chairman and Network Systems in connection with the acquisition. While Vitalink and Network Systems said they still believe the claims asserted are without merit, they said they agreed to the settlement to avoid further expense and distraction from the lawsuits.

- The settlement provides that Network Systems' option, under certain circumstances, to acquire slightly less than 20 pc of Vitalink's outstanding common stock will be amended to permit Vitalink to cancel the option by making a cash payment. Any such payment, and any payment in connection with Network Systems' election to cancel the option, will not exceed $2.77 million.

The companies said the merger agreement will be amended to limit Vitalink's obligation to reimburse

Network Systems for its fees and expenses in certain circumstances to $1.75 million.

The suits were filed on May 13 by Vitalink shareholders who charged Vitalink's management with breaching its fiduciary duties.

12:05 PM

* * *

FILED UNDER SEAL

IN THE COURT OF CHANCERY OF
THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY

IN RE: VITALINK COMMUNICATIONS CORPORATION SHAREHOLDERS LITIGATION	Consolidated C.A. No. 12085

MEMORANDUM OF OBJECTORS
IN OPPOSITION TO PROPOSED SETTLEMENT

This memorandum is submitted on behalf of the following stockholders of Vitalink Communications Corporation ("Vitalink"): Charles L. Grimes, John D. Burton, Reed Rubin, Louise I. G. Ireland, Renate Winston (as Custodian for Hella Winston), William P. Wood, Jr., Louisa W. Ruby,[1] Charles Kelly, Gadfly Foundation, Inc., Fidelity Bank (as Custodian for Gordon W. Chaplin and as Custodian for Susan C. Sternberg) (collectively, the "Objectors"). The Objectors collectively owned 311,000 shares of Vitalink common stock prior to the July 1, 1991 merger (the "Merger") whereby Network Systems Corporation ("NSC") completed its two-step acquisition of all outstanding Vitalink stock.

The claims that the named plaintiffs and defendants seek to settle were asserted in a complaint filed on May 13, 1991, captioned *John P. McCarthy Profit Sharing Plan v. Vitalink Communications Corporation, Network Systems Corporation and Leslie Denend*, C.A. No. 12085, as well as

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[1] William P. Wood, Jr. and Louisa W. Ruby were beneficial owners of Vitalink common stock. Their shares were held by Cede & Co., the nominal owner of record.

several similar actions.[2] In those actions, plaintiffs purported to assert certain claims on behalf of a class of the common stockholders of Vitalink.[3] The complaints challenged the agreement between NSC and Vitalink, announced on May 7, 1991, for the acquisition by NSC of all outstanding Vitalink stock for $10.50 per share (the "NSC Acquisition").

The complaints alleged that the directors of Vitalink breached their fiduciary duties in agreeing to the NSC Acquisition and that NSC aided and abetted those breaches of duty. The complaints contended, among other things, that the $10.50 per share consideration to be received by the Vitalink stockholders is grossly inadequate. Plaintiffs also alleged in their complaints that defendants failed to take steps designed to ensure that the Vitalink stockholders receive the highest possible price for their stock. In addition, the complaints challenged the grant to NSC of a "lock-up" through the device of an option to purchase approximately 20% of the outstanding shares of Vitalink, which was exercisable by

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[2] By order dated May 28, 1991, this Court consolidated the above cited action with three other purported class actions challenging the acquisition of Vitalink by NSC.

[3] Pursuant to its order dated July 18, 1991, this Court provisionally certified a class comprised of all record or beneficial holders of common stock of Vitalink who held shares at any time during the period from and including May 6, 1991 to and including July 1, 1991, the effective date of the Merger (the "Class").

NSC if, among other things, Vitalink withdrew or modified its recommendation of acceptance of the NSC Acquisition. (*See* Rein Dep. Ex. 2 at 12).[4]

NSC formally announced its agreement with Vitalink to commence a tender offer for all outstanding shares of Vitalink stock (the "Tender Offer") on May 6, 1991, three days before the *McCarthy* action was commenced. The tender offer was commenced on May 13. Plaintiffs never asserted claims based on the material omissions and misleading statements contained in the documents disseminated to the Vitalink stockholders in connection with the NSC Acquisition. Nor did they require, as part of the settlement of these actions, that defendants correct those inadequate disclosures.

On May 29-30, just two weeks after the filing of the various class action complaints and following very limited discovery, the class representatives and the defendants executed a stipulation of settlement and dismissal. On July 1, 1991, after the tender offer closed, defendants consummated a merger which eliminated the remaining Vitalink stockholders, including the Objectors herein, who chose not to tender their shares. Thus, the decision to settle in May did not, and could not, take into consideration the claims of members of the class that defendants breached their fiduciary duties in connection with the July merger. Nonetheless, the proposed settlement would

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[4] All documents cited herein that were produced in discovery, except for those documents identified as exhibits to the depositions, are set forth as exhibits hereto. In addition, the depositions taken in this action, with exhibits, will be lodged with the Court.

unjustly extinguish the ability of class members to assert those claims.

Plaintiffs and defendants now seek this Court's approval of their agreement to settle all claims asserted on behalf of the Class, as well as all claims that could have been asserted. As discussed below, the members of the Class have meritorious claims which should not be extinguished – at least not in exchange for the completely illusory consideration offered by defendants. Finally, although no member of the Class has benefitted from the proposed settlement or will do so in the future, the proposed settlement threatens to force upon the class a broad release that will forever bar it from asserting any claims against the named defendants and others pertaining to a laundry list of subjects that were never vigorously explored by plaintiffs. Finally, in numerous crucial respects the record presented to the Court by the parties is far too undeveloped to justify approval of the proposed settlement.

This settlement is not fair to the class. This Court should decline any invitation to approve the defendants' efforts to be rid of this litigation by paying off the plaintiffs' attorneys, providing sham benefits to the class and cutting off forever the ability of the absent members of the class to pursue their rights.

* * *

III. THE CLASS POSSESSES VALID CLAIMS AGAINST DEFENDANTS, BOTH UNDER STATE AND FEDERAL LAW, BASED ON DEFENDANTS' MATERIAL OMISSIONS AND MISREPRESENTATIONS IN CONNECTION WITH THE TENDER OFFER AND NOTICE OF MERGER.

Under Delaware law, the directors of Vitalink owe a duty of complete candor to the Vitalink stockholders. *See, e.g., Smith v. Van Gorkom*, Del. Supr., 488 A.2d 858, 889-93 (1985); *Lynch v. Vickers Energy Corp.*, Del. Supr., 383 A.2d 278, 281 (1977); *Rosenblatt v. Getty Oil Co.*, Del. Supr., 493 A.2d 929, 944-45 (1985). In addition, under federal law, defendants are prohibited from making material misrepresentations or omissions in the offering documents, the 14D-9 filed by the Vitalink board of directors and the Notice of Merger. *See* 15 U.S.C. §78n(d)(4). The members of the class have strong claims against defendants for violations of both state and federal law as a result of their materially misleading statements and omissions of facts material to the Vitalink stockholders' decisions with respect to the acquisition of Vitalink by NSC.

The Offer to Purchase, the Schedule 14D-9 and the Notice of Merger all recite the fact that Kidder had opined that the transaction was fair to the Vitalink stockholders. The Offer to Purchase and the Schedule 14D-9, apparently the only documents received by the Vitalink stockholders with respect to the tender offer prior to the expiration of the offer, contain absolutely no discussion or summary of the valuation analyses performed by Kidder. No mention whatsoever. Most important, there is no summary of the various valuation ranges arrived at by Kidder or any mention of the inadequacies or limitations

of those methodologies, as discussed above and as conceded by defendants. That information clearly would have been material to a Vitalink stockholder in determining the appropriate weight to accord to the Kidder "fairness" opinion at the time of the tender offer.

Delaware courts consistently have recognized that any material limitations recognized by financial advisors in rendering fairness opinions must be disclosed to the stockholders. *See, e.g., Joseph v. Shell Oil Co.*, Del. Ch., 482 A.2d 335, 341-343 (1984); *Weinberger v. UOP*, Del. Supr. 457 A.2d 701, 712 (1983); *Eisenberg v. Chicago Milwaukee Corp.*, Del. Ch., 537 A.2d 1051, 1060 (1987); *Kahn v. United States Sugar Corp.*, Del. Ch., C.A. No. 7313, slip op. at 14-15, Hartnett, V.C. (Dec. 10, 1985). Here, the failure to disclose the many limitations in connection with Kidder's "fairness" opinion renders defendants' trumpeting of Kidder's opinion patently misleading.

Defendants implicitly recognized the materiality of such information by virtue of the fact that they included in the Notice of Merger, which was disseminated *after* consummation of the tender offer and *after* the acquisition by NSC of 100% of the outstanding stock of Vitalink, the following discussion:

> Prior to the execution of the Merger Agreement, Vitalink and NSC's respective financial advisors, Kidder Peabody & Co. Incorporated ("Kidder Peabody") and Salomon Brothers Inc. ("Salomon"), prepared various analyses for Vitalink and NSC, respectively, including, among other things, an analysis of market multiples for comparable companies, analyses of

prices paid in precedent transactions for companies in similar lines of business and discounted cash flow analyses. Kidder Peabody's market multiples analysis resulted in a range between $7.14 and $11.49 per share. Kidder Peabody's and Salomon's precedent transaction analyses resulted in ranges between $12.27 and $21.02 per share, and $13.40 and $20.81 per share, respectively, and Kidder Peabody's and Salomon's discounted cash flow analyses resulted in ranges between $9.50 and $11.75 per share, and $10.50 and $11.75 per share, respectively. Kidder Peabody informed Vitalink's Board of Directors that Kidder Peabody's precedent transactions analysis was not particularly applicable to the Merger Agreement because, in part, there had been relatively few recent transactions in the networking industry and the comparable transactions analyzed by Kidder Peabody all had occurred between 1987 and 1989, a period in which transactions were valued differently. Kidder Peabody also discussed with Vitalink's Board of Directors the fact that most of the acquired companies selected by Kidder Peabody had revenues which were growing, unlike Vitalink's revenues which in recent periods had been declining. With respect to the discounted cash flow analysis, Vitalink's Board of Directors and Kidder Peabody had questioned the likelihood of achieving, and risks involved in the assumptions underlying, the projections on which such analysis was based, particularly in that projected future revenue growth was dependent on new product development that was no longer on schedule. Salomon, in its discounted cash flow analysis, utilized the same projections. Summaries of

> these projections were previously disclosed in the Offer to Purchase.

(Exhibit B at 6). There is absolutely no comparable disclosure in the Offer to Purchase or in the 14D-9.

Nor is there any disclosure in any of the documents disseminated to the Vitalink stockholders that the board of directors chose not to solicit bids from third parties other than NSC. The opinion of the Supreme Court in *Barkan* highlights the critical importance of such a market check to confirm the fairness of a proposed transaction. At a minimum, defendants were under an obligation to disclose that they had not done so and to explain their rationale for acting as they did.

Indeed, when the Kidder bankers working on the NSC Acquisition prepared an internal memorandum for review by the Kidder "Fairness Opinion Committee," they stated at the outset of that three-page memorandum that "Kidder has not been requested to, and did not, solicit third party indications of interest in acquiring all or any part of the Company." (Doc. No. KP000806). Similarly, an earlier draft of the Kidder fairness opinion contained the sentence: "[W]e have not been requested to, and did not, solicit third party indications of interest in acquiring all or any part of the company." A copy of that document was produced in the litigation with a line drawn through that very sentence. (Doc. No. KP000511, attached hereto as Exhibit D). The Kidder opinion actually disseminated to the Vitalink stockholders, however, did not contain any reference to the fact that Kidder had not solicited third party indications of interest. That opinion was one of only 2 of the 24 exhibits to the Vitalink

Schedule 14D-9 actually distributed to the Vitalink stockholders. Its importance to the Vitalink stockholders cannot be questioned. Nor can the importance of the omitted statement that no alternative offers were solicited be overstated.

The class has strong claims against defendants based on their failure to disclose these clearly material facts. These claims, while not even asserted by the class representatives, would be extinguished by virtue of the proposed settlement. This Court should not sanction that result – at least based on the illusory consideration offered the class members in this settlement.

* * *

In The
UNITED STATES COURT OF APPEALS
For The Third Circuit

No. 93-1268

C. L. GRIMES and G. W. HOLBROOK, on their own behalf and on behalf of all persons similarly situated,

Appellants,

v.

VITALINK COMMUNICATIONS CORPORATION, NETWORK SYSTEMS CORPORATION, LESLIE L. DENEND, J. DANIEL McCRANIE, CHARLES J. ABBE, HARRY T. REIN and LYLE D. ALTMAN,

Appellees.

BRIEF FOR APPELLANTS

Appeal from the Order dated February 27, 1993 of the United States District Court for the Eastern District of Pennsylvania in Civil Action No. 92-2722

Thaddeus Holt
c/o KITTREDGE, DONLEY,
ELSON, FULLEM & EMBICK
421 Chestnut Street - 5th Floor
Philadelphia, PA 19106
(215) 829-9900

Attorney for Appellants

* * *

forum or consents to jurisdiction.' " Addendum 6, App. 564. But the relevance of "minimum contacts" in *Real Estate Title* was with respect to personal jurisdiction over the class member for purposes of enjoining the collateral attack. The discussion of the right to collateral attack as "integral to the constitutionality of the class action procedure" in no way depends on whether or not the collateral attacker had "minimum contacts" with the class action forum. (Indeed, the fountainhead case, *Hansberry v. Lee*, 311 U.S. 32 (1940), dealt with real property in Illinois, and real property is the classic basis for "minimu contacts.")

The court below should really have referred not to *Real Estate Title* but to *Phillips Petroleum, supra,* for the court below held that Holbrook could be involuntarily bound in a non-opt-out class because he was "subject to the [personal] jurisdiction of the Delaware courts." It based this merely on Holbrook's owning stock in a Delaware corporation,[18] citing *Hynson v. Drummond Coal Co., Inc.*, 601 A.2d 570 (Del. Ch. 1991). Addendum 6, App. 564. This is plainly wrong. *Hynson* very carefully restricted jurisdiction over non-resident stockholders only "to the limited extent necessary to adjudicate their rights as stockholders against the corporation's directors and controlling shareholder" under "the equitable duty of loyalty created by the law of the incorporating state." 601 A.2d at 572, 580. *Hynson* holds *at most* only that a state court can

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[18] It said Holbrook had purchased stock *"from"* Vitalink. Addendum 6, App. 564. There is no evidence of this and the court presumably meant *"in"* Vitalink.

exercise jurisdiction over all parties in a determination of *internal* corporate rights and duties. But what is here involved is rights and duties *external* to the corporation, growing out of failure to disclose information in the purchases of shares by an outsider. A Connecticut citizen cannot, in the language of *World-Wide Volkswagen Corp. v. Woodson*, 444 U.S. 286, 297 (1980), "reasonably anticipate being haled into court" in Delaware with respect to an offer to buy his shares by a Minnesota-based entity; he has "purposefully availed himsef" of no "privilege of conducting activities" in Delaware with respect to purchase and sale of stock. *Hanson v. Denckla*, 357 U.S. 235, 243 (1958); see *Burger King Corp. v. Rudewicz*, 471 U.S. 462 (1985); *De James v. Magnificence Carriers, Inc.*, 654 F.2d 280 (3d Cir.), *cert. denied*, 454 U.S. 1085 (1981). Otherwise millions of daily Wall Street transactions would all be subject to Delaware jurisdiction.

* * *